



Sunrise

Wednesday, 13 January 2016

Rates: Risk sentiment, oil prices and supply

Core bonds erased all intraday losses during US dealings yesterday as oil prices suffered another blow. Amid a nearly empty eco calendar today, bond markets will be driven by the same forces as yesterday: risk sentiment, heavy bond supply and oil prices. We hold a neutral view.

Currencies: dollar ekes out marginal gains as China tensions ease

Yesterday, the dollar gained marginally ground as uncertainty on China receded. This morning, the dollar rebounds further as investors draw comfort from good Chinese foreign trade data. Later today, there are few eco data in the US and Europe. So, USD trading might develop more or less according to yesterday's trading pattern.

Calendar

Headlines

S&P	↗
Eurostoxx50	↗
Nikkei	↗
Oil	→
CRB	→
Gold	↘
2 yr US	→
10 yr US	↘
2 yr EMU	→
10 yr EMU	→
EUR/USD	↘
USD/JPY	↗
EUR/GBP	→

- **US Equities** ended their losing streak yesterday. The S&P rose 0.78% led by technology shares and the health care sector. **This morning, most Asian shares trade in positive territory.** Chinese stocks underperform, losing up to 2%.
- **China's trade surplus widened more than expected in December to \$60.09 billion, with both exports and imports falling less than expected.** Exports fell by 1.4% Y/Y from -6.8% Y/Y in November, suggesting that the weaker yuan is starting to support the country's export sector.
- **Further rate hikes by the US Federal Reserve should be gradual** and supported by clear evidence of inflation in the US or they risk hurting already fragile emerging economies, where many companies borrow in dollars, IMF Chairwoman **Lagarde** said yesterday.
- **Iran detained two US Navy boats and was holding 10 American crew members in the Persian Gulf,** US officials said yesterday, an incident which rattles nerves days before the expected implementation of the landmark nuclear accord.
- **The Brent oil price was hit by a new selling wave at the start of the US session yesterday.** The Brent closed below \$31/barrel and continues to trade around those levels this morning. **Gold** (\$1085/ounce) is trading lower this morning, for a fourth consecutive session, as market turmoil eased, slowing safe haven demand.
- Today, the **eco calendar** contains the **euro zone industrial production data** and several national inflation data in Europe. The Fed will publish its **Beige Book** and Fed's Rosengren & Evans and ECB's Lautenschlaeger are scheduled to speak.

Rates

Core bonds in rollercoaster with oil

Core bonds end session higher, despite intraday correction lower.

Oil rebound short-lived

	US yield	-1d
2	0,9395	0,0039
5	1,5643	-0,0181
10	2,1295	-0,0300
30	2,9024	-0,0516

Eco calendar unattractive.

Central bankers & Beige Book wildcards.

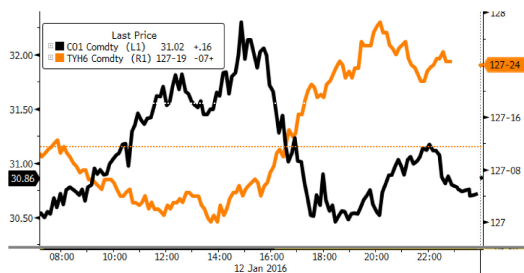
	DE yield	-1d
2	-0,3820	0,0020
5	-0,1045	0,0092
10	0,5365	-0,0074
30	1,3575	-0,0438

Discussion on ECB inflation target unlikely, but fiscal policy tool may come into focus if eco growth would ease.

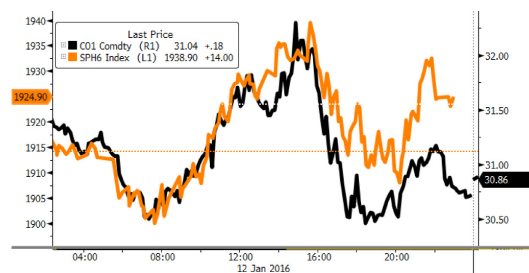
Global core bonds had a roller-coaster ride dancing a tango with oil prices. Global bonds initially declined on a pronounced rise of oil prices. Higher equities and heavy issuance also weighed at that stage. Core bonds took a turn for the better around 4 pm CET as oil prices retested the lows. US Treasuries ended with nice gains, outperforming German Bund. In a daily perspective, the US yield curve bull flattened with yields 0.8 bps to 8.7 bps lower. German yields were little changed until the 5-yr tenor and 0.8 bps (10-yr) to 3.5 bps (30-yr) lower at the longer end. On intra-EMU bond markets, 10-yr yield spread versus Germany widened up to 5 bps. The Spanish syndication (€9B Apr2026) was successful and Spain didn't concede ground versus its peer Italy. ECB speakers didn't influence markets. During US dealings, the NFIB Small Business Optimism slightly exceeded expectations but didn't weigh further on bonds.

The **eco calendar** contains the **EMU industrial production** data and several national European inflation data. In the US the Fed publishes **its Beige Book**. Fed's Rosengren and Evans, both doves, are scheduled to speak as well as ECB's Lautenschlaeger. Following a rebound in October, **EMU industrial production** is expected to show a limited drop in November. The consensus is looking for a decline by 0.3% M/M. We believe that the **risks are for a weaker outcome** following disappointing German, French and Spanish data. Part of the weakness will probably be based in utilities due to unusually warm weather, but also manufacturing activity probably remained poor.

ECB Vasiliauskas said the ECB should better focus on core inflation, but **Noyer** in his farewell address defended the inflation objective. ECB Chief Economist Peter **Praet** said there would be no change in monetary policy, as change would mean abandoning the 2% inflation target. In other concerns, **he sounded pessimistic saying that low inflation offers little buffer against deflation. Deflation means the ECB would lose control on real rates. With the oil price sliding further, the prospect of lower inflation for longer is obvious.** The ECB is now short of ammunition to fight low inflation. So, it is no surprise that some governors start wondering whether the ECB should target core inflation which is easier to affect than oil-driven headline inflation. They probably fear the ECB will be sucked deeper into unconventional policy with a still lower negative deposit rate or more QE. However, we don't expect a change in the target soon. **More likely, the focus will go to stimulating fiscal policy. Given the high debt levels and German aversion towards higher deficits, that discussion won't be easy.**



T-Note future (orange) and Brent future (black): Nice inverse relationship between oil price and bonds



S&P (orange) and oil (black): Equities shadow oil higher, drop when oil goes lower, but manage to take distance later on

R2	161,71	-1d
R1	160,66	
BUND	159,42	0,1400
S1	156,4	
S2	154,54	

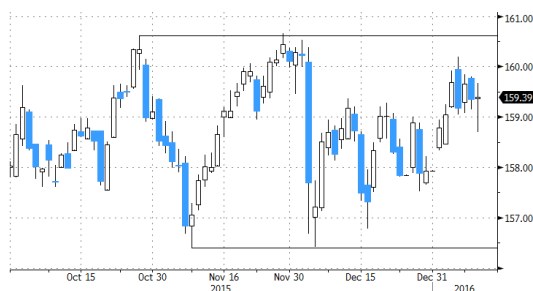
Heavy supply with new 10-yr OLO (Jun2026)

The Belgian debt agency will most likely launch a new 10-yr benchmark (OLO 77 Jun2026) after yesterday's delay. Concerning the pricing of the new OLO 77 (1% (?) Jun2026) on the Belgian yield curve, we interpolate asset swap spreads between OLO 74 (0.8% Jun2025) and OLO 75 (1% Jun2031) to calculate fair value. We didn't use OLO 64 (4.5% Mar2026) and OLO 31 (5.5% Mar2028) because they trade a tad special given their off-the-run status (especially OLO 31). Based on yesterday's closing levels, the interpolation corresponds with an asset swap spread of 8 basis points. This corresponds with a 1.01% yield to maturity. **The German Finanzagentur** launches a new 10-yr Bund (€5B 0.5% Feb2026). Grey market trading suggests that the bond will be priced to yield MS -30.3 bps, which is a 0.4 bps pick-up in ASW spread terms over the previous Bund (1% Aug2025). In yield terms, it's a 6 bps pick-up. Overall, we fear that demand for the Bund will remain rather weak. **The Italian debt agency** taps the on the run 3-yr BTP (€1.5-2B 0.30% Oct2018), 7-yr BTP (€2.5-3B 1.45% Sep2022) and 15-yr BTP (€1.25-1.75B 1.65% Mar2032). The bonds cheapened significantly going into the auction. On the Italian curve, the Mar2032 BTP trades very rich which could hamper demand for that bond. **In the US, the Treasury started its mid-month refinancing operation** with a mixed \$24B 3-yr Note auction. The bid cover was light, but the auction stopped firmly below the 1:00 PM bid side. Today, the US Treasury holds a \$21B 10-yr Note auction. WI trades at 2.13%.

Supply, risk sentiment and oil prices: difficult mix

Overnight, most Asian equities trade positive with Japan outperforming (+2%) and China underperforming (flat). The US Note future trades off yesterday's high reached in US dealings on a new crash of oil prices.

Today, the eco calendar is unlikely to rock markets with outdated EMU IP data and dovish FOMC governors (Evans, Rosengren). Overall, we hold a **more neutral view for today as similar factors as yesterday are at play. The devaluation of the renminbi stopped this week and this halted safe haven trades.** Apart from the Chinese side of the story, **markets also have to digest huge bond supply (apart from sovereigns probably also \$30B AB Inbev deal)**, which is also negative for bonds. **Continued weakness in the oil price** might dampen the downside though. At the start of the week, we've **put our sell-on-up ticks strategy on hold, at least until risk sentiment improves again.** Longer term, we believe that policy action by the ECB (failing to deliver on expected easing) and the Fed (start tightening cycle) puts a bottom below yields.



German Bund: Sideways trading range.



US Note future: Dovish reaction on payrolls suggests that Asian/Chinese turmoil is key for markets at this stage.

Currencies

Dollar little changed as China tensions ease further

Dollar recording marginal intraday gains but end nearly unchanged.

R2	1,106	-1d
R1	1,097	
EUR/USD	1,083	-0,0050
S1	1,0711	
S2	1,0524	

Sentiment on risk improves further

PBOC keeps yuan fixing again little changed

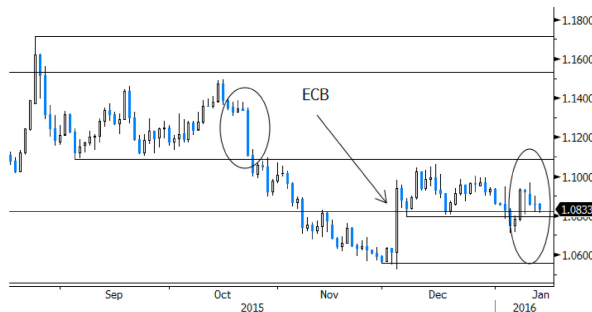
Eco calendar unattractive

Technical dollar trading likely

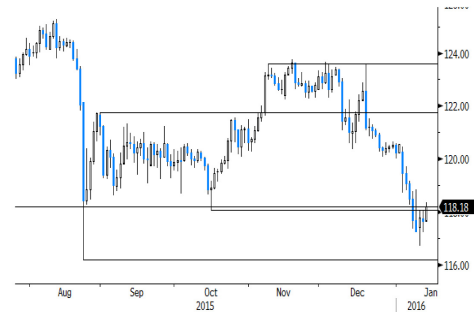
On Tuesday, the negative impact from the China crisis on global markets eased. However, the risk-on recovery was uneven across markets. Equities rebounded nicely. Oil initially rallied sharply, but gave back all gains later on in the US session. Similarly, core bonds were at first sold, but recouped losses and US Treasuries even closed handsomely higher. The dollar hovered on both sides of the opening levels to close nearly unchanged. EUR/USD declined from the 1.09 area early in European trading, up from an Asian start around 1.0856, to close the session at 1.0858 (unchanged for the day). USD/JPY tested the 118 area, but failed to sustain above that level. The pair ended the day at 117.65, even marginally lower from Monday's 117.76 close.

Overnight, most Asian equity markets show decent gains. Chinese indices underperform and are nearly flat. Investor sentiment improved further as the Chinese December trade surplus was much bigger than expected. The PBOC kept the yuan fixing little changed for the fourth day in a row. The off-shore yuan gained again a few ticks. There is also market talk that Chinese authorities instructed local banks to limit yuan outflows and to diminish positions in off shore yuan in order to stabilize the currency market and to limited the spread between the on shore and the off shore yuan. Oil rebounds slightly after setting a new correction low (WTI < \$30/pb)yesterday. The dollar records modest gains against the yen and the euro. USD/JPY trades currently in the 118.25 area. EUR/USD is changing hands in the 1.0834 area. Commodity currencies like the Aussie dollar and the Canadian dollar try to move away from the recent lows, but the gains are limited (especially for the cad), as commodities remain fragile.

Today, there are again few important eco data. The EMU production data are the exception to the rule, but a bit outdated (November series). So USD trading will again be driven by global market sentiment and by central bankers' comments (ECB's Lautenschlaeger and Fed members Rosengren and Evans) and the Beige Book.



EUR/USD: dollar slightly stronger as China tensions ease



USD/JPY: looking for a bottom

In a day-to-day perspective, uncertainty on China will likely ease further, a moderate dollar positive. However, yesterday's price action illustrates that a rebound in equities is no guarantee for higher core bond yields nor for big USD gains. So dollar gains might stay modest even if the equity rebound continues.

In this respect, it will be difficult for the dollar to break the downside of the 1.07/1.10 short-term trading range short-term. The China crisis is (temporary?) easing but might easily resurface, as Chinese authorities' policy response still relies on 'artificial' measures limiting market activity. In this context, we still look/prefer to sell EUR/USD higher in the trading range (closer to 1.10/1.11).

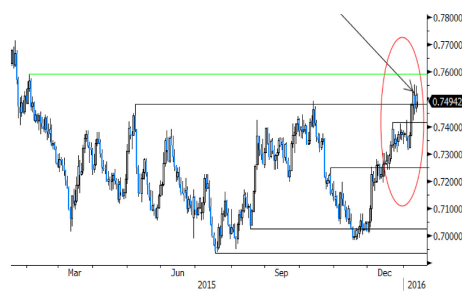
From a technical point of view, EUR/USD failed to regain important resistances at 1.1087 (breakdown) and 1.1124 (62% retracement from the October high). Last week, EUR/USD failed to sustain below 1.0796 support (07 Dec low). Next support is at 1.0650 (76% retracement off 1.0524/1.1060) and at 1.0524. On the topside, 1.1004 (reaction top) is a first reference. Next resistance comes in at 1.1060/1.1124 (15 Dec top/62% retracement) **The picture for USD/JPY remains negative below 120**. Next support comes in at 116.18 (August low). The pair moved into oversold territory and now tries to put a bottom in place .

R2	0,7593	-1d
R1	0,7555	
EUR/GBP	0,7494	0,0003
S1	0,7421	
S2	0,7313	

Cable sets another multi-year low

The constructive global risk sentiment didn't help sterling yesterday. On the contrary, **cable touched another multi-year low in the 1.4350/55 area**, the lowest level since June 2010. EUR/GBP also returned north of 0.75 even as EUR/USD declined on the global risk-on rebound. **The UK production data were to blame**. Manufacturing production even dropped -0.4% M/M and -1.2% Y/Y. The production data confirm the dichotomy in the UK economy. Decent domestic demand is partially offset by mediocre production and external trade. The data reinforced market expectations that the BoE will be soft at tomorrow's policy meeting and that and that sterling won't get additional interest rate support anytime soon. EUR/GBP closed the session at 0.7516 (from 0.7467 on Monday). Cable ended the day at 1.4448 (from 1.4543).

There are no important eco data in the UK today. So, the focus will be on tomorrow's **BoE policy meeting, BoE Minutes and on global market sentiment** . **Yesterday's data reinforced the case for a soft BoE assessment. A sustained GBP rebound will also remain difficult unless there is progress in the Brexit debate or unless risk sentiment improves**. That said, quite some bad news should already be discounted after the recent GBP decline. Especially cable was hit very hard. Was yesterday's sell-off in cable some kind of a short-term exhaustion move? Some short term consolidation might be on the cards especially if global market sentiment improves and the oil decline halts. The medium term picture of sterling against the euro remains negative as the pair broke above the 0.7493 Oct top. **Next resistance stands at 0.7593 (Feb 2015 top)**. Sterling is moving into oversold territory against the euro and the dollar, but it is no good enough a reason to rush into sterling longs yet.



EUR/GBP: test of the 0.75 area continues despite yesterday's sterling rebound



Cable holds near multi-year low

Calendar

Wednesday, 13 January		Consensus	Previous
US			
13:00	MBA Mortgage Applications	--	-11.6%
20:00	Monthly Budget Statement (Dec)	-\$10.0b	\$1.9b
Japan			
00:50	Money Stock M2 YoY (Dec)	A: 3.0%	3.3%
00:50	Money Stock M3 YoY (Dec)	A: 2.5%	2.7%
05:30	Bankruptcies YoY (Dec)	A: 1.89%	-3.39%
China			
	Trade Balance CNY/USD (Dec)	A: 382.05b/60.09b	343.1b/54.1b
	Exports YoY CNY/USD (Dec)	A: 2.3%/-1.4%	-3.7%/-6.8%
	Imports YoY CNY/USD (Dec)	A: -4.0%/-7.6%	-5.6%/-8.7%
EMU			
11:00	Industrial Production SA MoM/WDA YoY (Nov)	-0.3%/1.3%	0.6%/1.9%
France			
08:45	Current Account Balance (Nov)	--	-1.4b
08:45	CPI EU Harmonized MoM/YoY (Dec)	0.1%/0.2%	-0.2%/0.1%
Portugal			
12:00	CPI EU Harmonized MoM/YoY (Dec)	0.0%/0.6%	-0.4%/-0.6%
Greece			
11:00	CPI EU Harmonized YoY (Dec)	0.2%	-0.1%
Norway			
10:00	House Price Index QoQ (4Q)	--	1.2%
Sweden			
08:00	PES Unemployment Rate (Dec)	--	4.1%
Events			
11:05	Norway - Bond auction (NOK3B 1.75% Mar2025)		
11:10	Italy - BTP (€1.5-2B 0.3% Oct2018, €2.5-3B 1.45% Sep2022) & CCTeu (€1.25-1.75B 1.65% Mar2032) auction (11:10)		
11:30	Germany - Bund Auction (Eur 5bn Feb 2026) (11:30)		
12:00	ECB Executive Board Member Lautenschlaeger Speaks in Frankfurt		
12:00	BoE's Bailey speaks in Panel in London		
14:00	Fed's Rosengren Speaks on Economic Outlook to Boston Chamber		
18:30	Fed's Evans Speaks on Economy and Monetary Policy in Iowa		
19:00	US - 10Yr Note Auction (Usd 21bn) (19:00)		
20:00	U.S. Federal Reserve Releases Beige Book		

10-year	td	-1d	2-year	td	-1d	STOCKS	-1d
US	2,13	-0,03	US	0,94	0,00	DOW	16516 16516,22
DE	0,54	-0,01	DE	-0,38	0,00	NASDAQ	for Exch - NQJ #VALUE!
BE	0,90	0,00	BE	-0,34	0,01	NIKKEI	17716 17715,63
UK	1,75	-0,02	UK	0,48	-0,02	DAX	9985,43 9985,43
JP	0,21	-0,01	JP	-0,02	0,00	DJ euro-50	3065 3064,66

						USD	td	-1d
IRS	EUR	USD (3M)	GBP	EUR	-1d	-2d	Eonia EUR	-0,233 0,003
3y	-0,008	1,182	1,063	Euribor-1	-0,22	0,00	Libor-1 USD	0,51 0,51
5y	0,241	1,472	1,337	Euribor-3	-0,14	0,00	Libor-3 USD	0,59 0,59
10y	0,880	1,957	1,777	Euribor-6	-0,05	0,00	Libor-6 USD	0,75 0,75

Currencies		-1d	Currencies		-1d	Commoditie	CRB	GOLD	BRENT
EUR/USD	1,083	-0,0056	EUR/JPY	127,97	0,26		164,2365	1084,76	31
USD/JPY	118,2	0,85	EUR/GBP	0,7494	0,0003	-1d	0,00	-9,59	0,36
GBP/USD	1,4444	-0,0082	EUR/CHF	1,0881	0,0004				
AUD/USD	0,7019	0,0059	EUR/SEK	9,2527	-0,02				
USD/CAD	1,4246	0,0009	EUR/NOK	9,6192	-0,10				

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